

**STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR**

JUNE 30, 2006



**AUDITED FINANCIAL STATEMENTS,
MANAGEMENT'S DISCUSSION AND ANALYSIS,
SUPPLEMENTARY DATA AND
AUDITORS' REPORT ON INTERNAL CONTROL,
COMPLIANCE AND OTHER MATTERS**

PHIL BRYANT
State Auditor

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
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INDEPENDENT AUDITORS' REPORT

Principals

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Lacie A. Myers, CPA
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William F. Taylor, CPA
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Melanie S. Woodrick, CPA

State of Mississippi
Office of the State Auditor
Jackson, Mississippi

We have audited the accompanying financial statements of the governmental activities and the agency fund information of the State of Mississippi Office of the State Auditor as of and for the year ended June 20, 2006, which collectively comprise the basic financial statements as listed in the table of contents. These financial statements are the responsibility of the State of Mississippi Office of the State Auditor's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatements. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the significant estimates made by management, as well as an evaluation of the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities and the agency fund information of the State of Mississippi Office of the State Auditor as of June 30, 2006, and the changes in its net assets for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 20, 2006, on our consideration of the State of Mississippi Office of the State Auditor's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control of financial reporting and

compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information on pages 3 through 9 and pages 25 and 26, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Grantham, Poole, Rundell, Reitano, Arrington & Cunningham, PLLC

Jackson, Mississippi
October 20, 2006

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Management's Discussion and Analysis
Year Ended June 30, 2006

The following discussion and analysis of the Office of the State Auditor's (OSA) financial performance provides an overview of the OSA's financial activities for the fiscal year ended June 30, 2006. Readers are encouraged to consider the information presented here in conjunction with the OSA's financial statements, which immediately follow this discussion and analysis.

Financial Highlights

Government-wide – The assets of the OSA exceeded its liabilities at the close of the fiscal year by \$1,023,870 (reported as “net assets”). Of this amount, \$984,808 was reported as “unrestricted net assets”, which may be used to meet the OSA's ongoing obligations. Net assets increased by \$3,082 from the previous year.

Fund level – As of the close of the fiscal year, the OSA's governmental fund reported an ending fund balance of \$1,367,753, which is a decrease \$104,649 from the previous year.

Overview of the Financial Statements

This discussion and analysis serves as an introduction to the OSA's basic financial statements, which include government-wide financial statements, fund financial statements and the notes to the financial statements. This report also contains required supplementary information.

Government-wide Financial Statements

The government-wide financial statements are designed to provide the reader with a broad overview of the OSA's finances. These statements consist of the statement of net assets and the statement of activities, which are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. The current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The statement of net assets presents information on all the OSA's nonfiduciary assets and liabilities, with the differences between the two reported as “net assets”. Over time, increases or decreases in the OSA's net assets may serve as a useful indicator of whether its financial position is improving or deteriorating.

The statement of activities presents information showing how the OSA's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., earned but unused vacation leave).

The OSA has only one kind of activity reported in the government-wide financial statements.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Management's Discussion and Analysis
Year Ended June 30, 2006

Governmental Activities: All of the OSA's services are reported in the governmental activities. These activities are primarily financed by appropriations from the State of Mississippi and fees charged for services provided.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. These categories use different accounting approaches and should be interpreted differently.

Governmental Fund: The OSA's activities are reported in a governmental fund. The governmental fund is used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, the governmental fund is accounted for using the modified accrual basis of accounting and the flow of current financial resources measurement focus. This approach focuses on near-term inflows and outflows of spendable resources, as well as balances of spendable resources available at year end. The governmental fund statements provide a detailed view of the OSA's near-term financing requirements. All of the governmental fund activities of the OSA are accounted for as a General Fund.

Because the focus of the governmental fund is narrower than that of the government-wide financial statements, it may be useful to compare the information presented for the governmental fund with similar information presented for governmental activities in the government-wide financial statements. By doing so, the reader may gain a better understanding of the long-term impact of the OSA's near-term financing decisions. Both the governmental fund balance sheet and statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between the governmental fund and governmental activities.

Fiduciary Fund: A fiduciary fund is used to account for resources held for the benefit of parties outside the OSA. Because these resources are not available to support the OSA's own programs, the fiduciary fund is not reported in the government-wide financial statements. The OSA's fiduciary activities are presented in a statement of fiduciary net assets. This fund is reported using the accrual basis of accounting.

Notes to the Financial Statements

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found immediately following the statement of fiduciary net assets.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Management's Discussion and Analysis
Year Ended June 30, 2006

Other Information

This report also contains a Budgetary Comparison Schedule – Budget and Actual (non-GAAP Basis) – General Fund, along with the accompanying notes, which is required supplementary information.

Government-wide Financial Analysis

Net Assets

During fiscal year 2006, the OSA's total net assets increased by \$3,082 or 0.3 percent from the previous year. In contrast, net assets in the prior year increased by \$13,881 or 1.4 percent.

The largest portion of net assets, 96.2 percent, consists of unrestricted net assets. Unrestricted net assets decreased \$30,742 from the previous year. The decrease was caused primarily by a reduction in revenues.

	Net Assets Governmental Activities	
	2006	2005
Current and other assets	\$ 1,714,929	\$ 1,781,491
Capital assets	75,315	58,742
Total assets	<u>1,790,244</u>	<u>1,840,233</u>
Current liabilities	287,325	326,340
Noncurrent liabilities	479,049	493,105
Total liabilities	<u>766,374</u>	<u>819,445</u>
Net assets:		
Invested in capital assets, net of related debt	39,062	5,238
Unrestricted	984,808	1,015,550
Total net assets	<u>\$ 1,023,870</u>	<u>\$ 1,020,788</u>

Changes in Net Assets

As a result of the excess of revenues over expenses, the OSA's net assets increased by \$3,082 or 0.3 percent during fiscal year 2006. Appropriations from the State provided \$5,277,475, or 58.6 percent of the OSA's total revenues, while 34.2 percent resulted from charges for services, and

STATE OF MISSISSIPPI
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Management's Discussion and Analysis
Year Ended June 30, 2006

4.3 percent from an operating grant. Salaries and benefits made up \$7,147,455 or 79.4 percent of the OSA's expenses, with 7.4 percent spent for travel and subsistence, and 11.1 percent for contractual services. In the prior year, appropriations from the State provided \$5,722,582, or 62.5 percent of the OSA's total revenues, while 36.1 percent resulted from charges for services and 0.4 percent from an operating grant. In addition, salaries and benefits were 81.2 percent of the OSA's expenses, with 6.9 percent spent for travel and substance, and 9.3 percent for contractual services.

Change in Net Assets
Governmental Activities

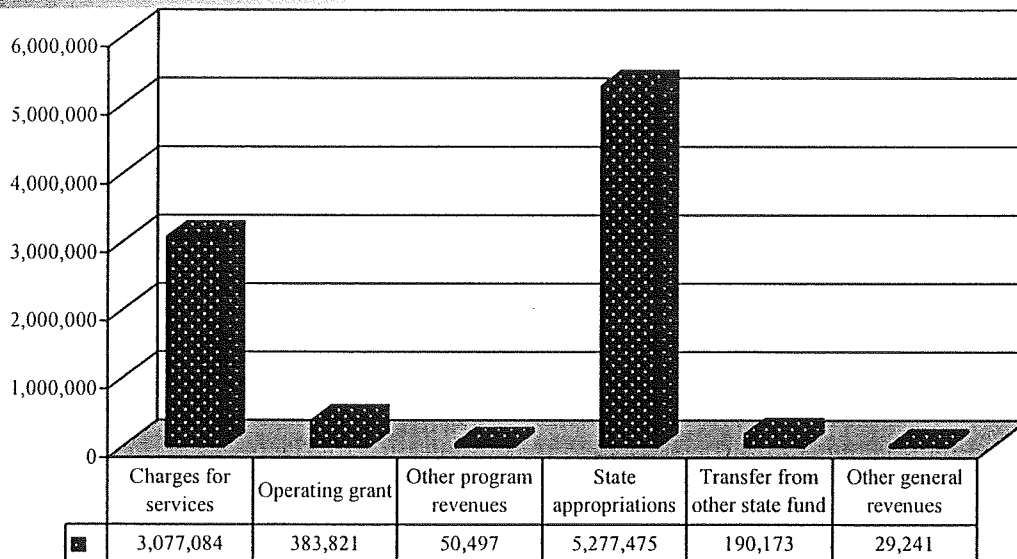
	<u>2006</u>	<u>2005</u>
Revenues:		
Program revenues:		
Charges for services	\$ 3,077,084	\$ 3,306,074
Operating grant	383,821	38,830
Other	50,497	87,180
General revenues:		
State appropriations	5,277,475	5,722,582
Transfer from other state fund	190,173	1,848
Other	29,241	
Total Revenues	<u>9,008,291</u>	<u>9,156,514</u>
Expenses:		
Personal services:		
Salaries and benefits	7,147,455	7,424,242
Travel and subsistence	667,268	632,454
Contractual services	1,000,191	849,540
Commodities	112,224	79,494
Interest expense	1,634	2,193
Noncapitalized machinery and equipment	53,133	25,919
Depreciation expense	23,304	128,791
Total expenses	<u>9,005,209</u>	<u>9,142,633</u>
Change in Net Assets	3,082	13,881
Net Assets – Beginning	1,020,788	1,006,907
Net Assets - Ending	\$ <u>1,023,870</u>	\$ <u>1,020,788</u>

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
 Management's Discussion and Analysis
 Year Ended June 30, 2006

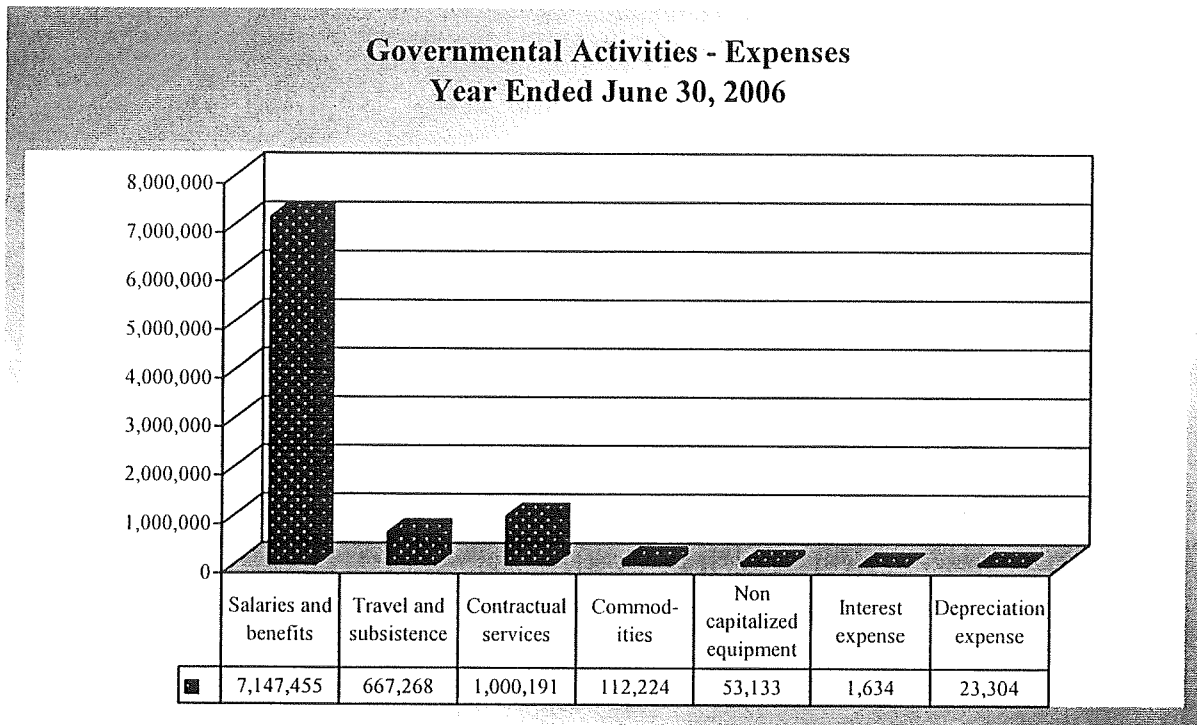
Governmental Activities

Governmental activities increased the OSA's net assets by \$3,082. Contributing factors to this increase are the reduction in charges for services and state appropriations, and the reduction in funded staff positions by the Legislature, which resulted in a decrease in salaries and benefits of \$276,787. The \$228,990 decrease in charges for services is partially attributable to this same factor, as the unfunded positions result in fewer billable hours for services provided.

Governmental Activities - Revenues
Year Ended June 30, 2006



**STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Management's Discussion and Analysis
Year Ended June 30, 2006**



Financial Analysis of the OSA's Governmental Fund

As noted earlier, the OSA uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Fund

The governmental fund (General Fund) reported a fund balance of \$1,367,753 as of June 30, 2006, a decrease of \$104,649 as compared to the prior year. Of this amount, \$1,335,814 or 97.7 percent constituted unreserved-undesignated fund balance.

Revenues decreased by 2.5 percent, or \$230,239, and expenditures decreased by 1.4 percent, or \$127,386. The decrease in revenues was principally from a decrease in charges for services of \$281,765, a decrease in state appropriations of \$445,107, and an increase of \$344,991 in federal sub-grant over the previous year. This can primarily be attributed to a reduction in funding for staff positions by the Legislature and a federal sub-grant related to cyber security audits. The decrease in expenditures of \$280,559 for salaries and benefits is primarily attributed to a reduction in funding for staff positions by the Legislature. As a result, the OSA utilized funds on hand in order to meet excess expenditures.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Management's Discussion and Analysis
Year Ended June 30, 2006

General Fund Budgetary Highlights

The original estimated amount for General Fund revenues and expenditures were revised for federal sub-grant funds received from other state agencies.

The following summarizes the significant items impacting the budgetary amounts:

Revenues from charges for services were \$1,527,484 below its budgeted amount and revenues from federal sub-grant were \$347,349 below its budgeted amount.

Expenditures for salaries and benefits were \$1,328,608 below its budgeted amount and expenditures for contractual services were \$311,354 below its budgeted amount.

Capital Assets

The OSA's investment in capital assets for its governmental activities as of June 30, 2006, amounted to \$428,493, less accumulated depreciation of \$353,178, resulting in a net book value of \$75,315. This reflects a net increase for the current year of 28.2 percent, compared to the prior fiscal year's decrease of 6.5 percent. Depreciation expense for the fiscal year 2006 totaled \$23,304 for governmental activities.

**Capital Assets, Net of Depreciation
Governmental Activities**

	<u>2006</u>	<u>2005</u>
Machinery and equipment	\$ <u>75,315</u>	\$ <u>58,742</u>

Request for Information

This financial report is designed to provide our citizens, taxpayers, and Legislature with a general overview of the Office of the State Auditor's finances and to demonstrate the OSA's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact: Administrative Services Division, Office of the State Auditor, P.O. Box 956, Jackson, Mississippi 39205.

FINANCIAL STATEMENTS

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Statement of Net Assets
June 30, 2006

Assets

Current assets:

Cash	\$ 985,041
Petty cash	2,000
Accounts receivables (less allowance for doubtful accounts of \$972)	688,104
Advance to cafeteria plan	15,000
Loans to other funds	24,784

Total current assets	1,714,929
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Noncurrent assets:

Capital assets:

Machinery and equipment, net	75,315
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Total noncurrent assets	75,315
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Total assets	1,790,244
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Liabilities

Current liabilities:

Warrants payable	132,898
Accounts payable and accruals	128,691
Lease obligations payable	17,828
Due to other funds	7,908

Total current liabilities	287,325
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Noncurrent liabilities:

Lease obligations payable	18,425
Accrued compensated absences	460,624

Total noncurrent liabilities	479,049
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Net Assets:

Invested in capital assets, net of related debt	39,062
Unrestricted	984,808

Total net assets	\$ 1,023,870
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The accompanying notes to the financial statements are an integral part of this statement.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Statement of Activities and Changes in Net Assets
Year Ended June 30, 2006

Expenses

Salaries and benefits	\$ 7,147,455
Travel and subsistence	667,268
Contractual services	1,000,191
Commodities	112,224
Interest expense	1,634
Noncapitalized machinery and equipment	53,133
Depreciation expense	23,304

Total expenses	9,005,209
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Program Revenues

Charges for services	3,077,084
Operating grant	383,821
Other	50,497

Total program revenues	3,511,402
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General revenues

State appropriations	5,277,475
Transfer from other state fund	190,173
Other	29,241

Total general revenues	5,496,889
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Change in Net Assets	3,082
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Net Assets – Beginning	1,020,788
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Net Assets – Ending	\$ 1,023,870
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The accompanying notes to the financial statements are an integral part of this statement.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Balance Sheet – Governmental Fund
June 30, 2006

Assets

Cash	\$	985,041
Petty cash		2,000
Accounts receivables (less allowance for doubtful accounts of \$972)		610,425
Advance to cafeteria plan		15,000
Loans to other funds		24,784
Total assets	\$	<u>1,637,250</u>

Liabilities and Fund Balance

Liabilities:

Warrants payable	\$	132,898
Accounts payable and accruals		128,691
Due to other funds		7,908
Total liabilities		<u>269,497</u>

Fund balances:

Reserved for encumbrances		31,939
Unreserved – undesignated		1,335,814
Total fund balance		<u>1,367,753</u>
Total liabilities and fund balance	\$	<u>1,637,250</u>

The accompanying notes to the financial statements are an integral part of this statement.

**STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR**

Reconciliation of the Governmental Balance Sheet to the Statement of Net Assets
June 30, 2006

Fund balance for governmental fund	\$ 1,367,753
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Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and therefore are not reported in the fund:

Machinery and equipment, net	75,315
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Some revenues will be collected after year-end but are not available soon enough to pay for the current period's expenditures and therefore are deferred in the fund.	77,679
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Capital lease obligation liabilities are not due and payable in the current period and therefore are not reported in the fund.	(36,253)
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Accrued compensated absences liabilities and related accrued interest are not due and payable in the current period and therefore are not reported in the fund.	<u>(460,624)</u>
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Net assets of governmental activities	\$ <u>1,023,870</u>
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The accompanying notes to the financial statements are an integral part of this statement.

**STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR**

Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Fund
Year Ended June 30, 2006

Revenues

State appropriations	\$ 5,277,475
Transfer from other state fund	190,173
Charges for services	2,999,405
Federal sub-grant	383,821
Other	50,497

Total revenues	8,901,371
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Expenditures

Current:

Salaries and benefits	7,143,683
Travel and subsistence	667,268
Contractual services	1,000,191
Commodities	112,140
Debt service	
Principal	17,251
Interest	1,634
Noncapitalized capital outlay	53,133
Capitalized capital outlay	10,720

Total expenditures	9,006,020
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Net Change In Fund Balance	(104,649)
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Fund Balance – Beginning	1,472,402
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Fund Balance - Ending	\$ 1,367,753
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The accompanying notes to the financial statements are an integral part of this statement.

**STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR**

Reconciliation of the Governmental Funds Statement of Revenues, Expenditures,
and Changes in Fund Balance to the Statement of Activities and Changes in Net Assets
Year Ended June 30, 2006

Net change in governmental fund balance	\$ (104,649)
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Amounts reported for governmental activities in the statement of activities
are different because:

Governmental funds report capital outlay as expenditures. However,
in the statement of activities, the cost of capital assets is allocated over
their estimated useful lives as depreciation expense. In the current
period, these amounts are:

Capitalized capital outlay	10,720
Depreciation expense	(23,304)

Net changes in revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the fund.	106,920
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In the statement of activities, only gains and losses from the sale of capital assets are reported, whereas in the governmental funds, proceeds from the sale of capital assets increase financial resources.	(84)
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The repayment of the principal of long-term debt consumes the current financial resources of the governmental fund; however this transaction has no effect on net assets.	17,251
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Some items reported in the statement of activities do not provide or
require the use of current financial resources and therefore are not
reported as revenues/expenditures in governmental funds

Change in compensated absences	<u>(3,772)</u>
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Change in net assets of governmental activities	\$ <u><u>3,082</u></u>
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The accompanying notes to the financial statements are an integral part of this statement.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Statement of Fiduciary Net Assets – Agency Fund
June 30, 2006

Assets

Cash	\$	<u>99,187</u>
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Total Assets	\$	<u>99,187</u>
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Liabilities

Accounts payable and accruals	\$	46,686
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Due to local governments		<u>52,501</u>
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Total Liabilities	\$	<u>99,187</u>
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The accompanying notes to the financial statements are an integral part of this statement.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Notes to the Financial Statements
Year Ended June 30, 2006

Note 1 – Significant Accounting Policies

The significant accounting policies applicable to the Office of the State Auditor (OSA) are described below.

- A. Basis of Presentation** – The accompanying financial statements of the OSA have been prepared in conformity with accounting policies generally accepted in the United States of America (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB). GASB is the accepted standard-setting body for governmental accounting and financial reporting principles.
- B. Financial Reporting Entity** – The OSA is an agency of the State of Mississippi created by the Legislature for the primary purpose of performing financial and legal compliance post audits of state agencies, county governments, public school districts, colleges and universities. The OSA also provides the following services:
- Technical assistance to state and local government entities,
 - Investigate instances of embezzled, misspent or misappropriated public funds,
 - Verifies the validity and accuracy of the process and the internal controls for information recorded in the Mississippi Student Information System by public schools,
 - Reviews governmental entities to identify ways to improve fiscal and managerial performance, and
 - Review state and local governments to ensure public property is properly accounted for.

The OSA is subject to the review and appropriation authority of the Legislature. The OSA is not an autonomous entity, but is rather a part of the oversight unit of the State of Mississippi.

C. Government-wide and Fund Financial Statements

Government-wide Financial Statements – The Statement of Net Assets and Statement of Activities and Changes in Net Assets report information on nonfiduciary activities of the OSA. Governmental activities generally are financed through taxes, intergovernmental revenues and other non-exchange revenues.

The Statement of Net Assets is a statement of position, which presents all of the OSA's nonfiduciary assets and liabilities, with the difference reported as net assets. GAAP requires that net assets be subdivided into three categories:

- Invested in capital assets, net of related debt – capital assets net of accumulated depreciation and reduced by outstanding balances for notes and other debt that are attributable to the acquisition of those assets.
- Restricted net assets – assets, less any related liabilities, restricted externally by creditors, grantors, contributors, or imposed by law through constitutional provisions or enabling legislation. At June 30, 2006, there were no restricted net assets.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Notes to the Financial Statements
Year Ended June 30, 2006

- Unrestricted net assets – assets that are not classified as invested in capital assets, net of related debt or restricted net assets.

The Statement of Activities and Changes in Net Assets demonstrates the degree to which direct expenses of a given function are offset by program revenues. Direct expenses are those that are specifically associated with a service, program, or department and, thus, are clearly identifiable to a particular function. Certain indirect costs have been included as part of the program expenses reported for the various functions and activities. Program revenues include 1) charges to clients of a given function and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. General revenues include state appropriations and any sources of revenue that are not reported as program revenues.

Fund Financial Statements – Separate financial statements are provided for the governmental fund and the fiduciary fund. The major individual governmental fund is reported in the fund financial statements.

D. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using a current financial resources measurement focus and the modified accrual basis of accounting. Only current assets and current liabilities are generally included on the balance sheet. Revenues are recognized when measurable and available to finance operations of the current fiscal year. Available means collectible within the current year or soon enough after fiscal year end to liquidate liabilities existing at the end of the fiscal year. The OSA considers revenues received within 60 days after fiscal year end as available. Expenditures and related fund liabilities are recognized upon receipt of goods and services.

The OSA reports the following major governmental fund:

- The General Fund is the operating fund of the OSA. It accounts for transactions related to resources obtained and used for traditional government services provided by the OSA. Certain resources obtained from federal grants and used to support general government activities are accounted for in the General Fund consistent with applicable legal requirements.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Notes to the Financial Statements
Year Ended June 30, 2006

Additionally, the OSA reports the following fiduciary fund type:

- The Agency Fund accounts for audit exceptions that the OSA collects for others in an agency capacity.
- E. Receivables** – Receivables represent amounts due to the OSA for revenues earned that will be collected sometime in the future. Receivables are reported net of allowances for uncollectible accounts.
- F. Capital Assets** – Capital assets are reported, net of depreciation, in the governmental column in the government-wide financial statements. Purchased capital assets are reported at cost. Donated capital assets are recorded at their fair market value on the date of donation. The class of capital assets used by the OSA and its related capitalization threshold is machinery and equipment - \$5,000. The machinery and equipment capital assets are depreciated using the straight-line method over estimated service lives of 5 to 15 years for machinery and equipment, 3 years for computer equipment, and 3 years for vehicles.
- G. Risk Management – Claims Payable** – As an agency of the State, the OSA participates in the State's risk management practices. The State has elected to finance exposures to risk for health and life benefits, tort liability, unemployment benefits and workers' compensation benefits through the retention of risk. The OSA participates in the State's Risk Management Fund. A liability for a claim is established if information indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss is reasonably estimable.
- H. Accumulated Unpaid Personal Leave and Major Medical Leave** – State law authorizes payment for a maximum of 30 days accrued personal leave in a lump sum upon termination of employment. No payment is authorized for accrued major medical leave unless employees present medical evidence that their physical condition is such that they can no longer work in a capacity of state government.

The OSA's obligation for accumulated unpaid personal leave, up to the maximum of 30 days per employee, is reported in the government-wide financial statements. In the governmental fund, only the amounts that normally would be liquidated with expendable available financial resources are accrued as current year expenditures. The OSA uses the last-in, first-out method of recognizing use of compensated absences. The reported liability applicable to all funds includes the related fringe benefits that the OSA as employer is required to pay when the accrued compensated absences are liquidated.

Accumulated unpaid major medical leave is not accrued because it is not probable that the compensation will be paid in a lump sum other than in the event of severe illness.

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Notes to the Financial Statements
Year Ended June 30, 2006

- I. Net Assets/Fund Balance** – The difference between fund assets and liabilities is “Net Assets” on government-wide financial statements and “Fund Balance” on governmental fund financial statements.

The unreserved fund balance reflects the balance available to be used for the general purposes of the fund, within spending limits authorized by the Legislature.

- J. Federal Grants** – Federal reimbursement type grants are recorded as revenues when the related expenditures are recognized. Use of grant resources is conditioned upon compliance with terms of the grant agreements and applicable federal regulations, which include subjecting grants to financial and compliance audits.

Note 2 - Cash

Cash accounts consist of checking accounts with depository banks and treasury funds maintained with the Mississippi State Treasury, as required by law.

Note 3 – Capital Assets

Capital asset activity for the year ended June 30, 2006, was as follows:

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets being depreciated				
Machinery and equipment	\$ 396,961	\$ 39,961	\$ 8,429	\$ 428,493
Less accumulated depreciation for:				
Machinery and equipment	<u>338,219</u>	<u>23,304</u>	<u>8,345</u>	<u>353,178</u>
Capital assets, net	<u>\$ 58,742</u>	<u>\$ 16,657</u>	<u>\$ 84</u>	<u>\$ 75,315</u>

Note 4 – Long-term Liabilities

- A. Compensated Absences** – The OSA’s liability for compensated absences at June 30, 2006, was \$460,624. The reported liability includes related fringe benefits and excludes any obligations related to leave accumulations in excess of 30 days per employee (see Note 1-H).
- B. Capital Lease Commitments** – The OSA leased automobiles through the State’s master leasing program. The lease has the following terms:

Lease originated on April 16, 2003, with an annual interest rate of 3.32% and a principal amount of \$86,394. Payments are to be made over a five year period.

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Notes to the Financial Statements
Year Ended June 30, 2006

The lease contains a fiscal funding addendum stating that the lease shall be terminate on the last day of the fiscal year if appropriated funds for the ensuing fiscal year are insufficient.

The OSA is obligated for the following capital assets acquired through capital leases as of June 30, 2006:

Machinery and equipment	\$	86,394
Less: Accumulated depreciation		<u>77,755</u>
Leased property under capital leases	\$	<u><u>8,639</u></u>

At June 30, 2006, future minimum commitments under capital leases are:

<u>Year Ending June 30</u>		<u>Amount</u>
2007	\$	18,885
2008		18,885
Total minimum lease payments		<u>37,770</u>
Less interest		<u>1,517</u>
Present value of net minimum lease payments	\$	<u><u>36,253</u></u>

Note 5 – Changes in Long-term Liabilities

Changes in the OSA's long-term liabilities for the year ended June 30, 2006, are summarized below:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Capital lease obligations	\$ 53,504	\$ -	\$ 17,251	\$ 36,253	\$ 17,828
Accrued compensated absences	<u>456,852</u>	<u>353,415</u>	<u>349,643</u>	<u>460,624</u>	<u>-</u>
Total	\$ <u>510,356</u>	\$ <u>353,415</u>	\$ <u>366,894</u>	\$ <u>496,877</u>	\$ <u>17,828</u>

STATE OF MISSISSIPPI
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Notes to the Financial Statements
Year Ended June 30, 2006

Note 6 – Retirement Plan

Plan Description – The OSA contributes to the Public Employees' Retirement System of Mississippi (PERS), a cost-sharing, multiple-employer, defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments and death benefits to plan members and beneficiaries. Benefit provisions are established by state law and may be amended only by the State of Mississippi Legislature. PERS issues a publicly available financial report that includes financial statements and required supplementary information. That information may be obtained by writing to Public Employees' Retirement System, PERS Building, 429 Mississippi Street, Jackson, MS 39201-1005 or by calling 1-800-444-PERS.

Funding Policy - PERS members are required to contribute 7.25% of their annual covered salary, and the OSA is required to contribute at an actuarially determined rate. The current rate is 10.75% of annual covered payroll. The contribution requirements of PERS members are established and may be amended only by the Legislature. The OSA's contributions to PERS for the years ending June 30, 2006, 2005 and 2004 were \$557,102, \$567,503 and \$429,715, respectively, equal to the required contributions for each year.

Note 7 – Commitments

The OSA has entered into several agreements to lease buildings which are classified as operating leases. These agreements contain the provision that, at the expiration date of the lease, the OSA may renew the operating lease on a month-to-month basis. It is expected that in the normal course of business most of these leases will be renewed or replaced by similar leases. Future minimum commitments due under operating leases for buildings as of June 30, 2006, were as follows:

<u>Year Ending June 30</u>	<u>Amount</u>
2007	\$ 20,716
2008	20,916
2009	20,916
2010	<u>13,830</u>
Total Minimum Commitments	\$ <u>76,378</u>

Note 8 – Risk Management

The OSA is an agency of the State of Mississippi and falls under the State's risk management practices. The State has elected to finance most exposures to risk through the retention of risk. The exposures to risk retained by the State are health and life benefits, tort liability, unemployment benefits and workers' compensation benefits. The State utilizes the internal service Risk Management Fund to account for these activities.

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Notes to the Financial Statements
Year Ended June 30, 2006

Health and Life Benefits: The State has elected to manage the health benefit through the retention of all exposure. The life benefit is purchased from a commercial insurance company for death benefit distribution under tax law but management of the risk is accomplished by self insuring within an insured shell. State law mandates that all state, public education, library, junior and community college and retiring employees be offered health and life benefit coverage through this plan.

Estimates of the liabilities for incurred (both reported and unreported) but unpaid claims are actuarially determined using the development method. This method uses past observed patterns of time between claim incurral and payment to estimate incurred claims from available claims data. Liabilities are based on the estimated ultimate cost of settling the claims, including inflation and other factors, and provisions for estimated claims adjustment expenses.

Tort Liability: The State manages tort claims through the retention of all liability exposure. The Legislature created the Tort Claims Board to administer these claims beginning in fiscal year 1994. Statutory regulations provide some protection, as well as a limitation of liability, for claims filed against state agencies and state employees.

Claims payments are financed through an annual assessment to all state agencies based on amount of payroll and past loss history. Estimates of the liability for unpaid claims are actuarially determined based on observed patterns of claims payments, as well as the experience of similar programs in other states.

Unemployment Benefits: Unemployment benefits are established in statute and administered by the Mississippi Department of Employment Security. The State elects to manage the financial risk for state agencies through retention of all liability exposure. Benefits are financed through collection of premiums from agencies, which provides a stable cash flow for payment of claims.

Workers' Compensation Benefits: Workers' compensation benefits are established in statute and the rules and regulations are established by the Mississippi Workers' Compensation Commission and the Mississippi State Agencies Self-Insured Workers' Compensation Trust Board of Trustees. The exposure of risk is financed mostly through retention of all exposure, with limited purchase of commercial excess insurance. The benefits are financed through collection of premiums, based on an actuarial estimate, from agencies which provides a stable cash flow for claims payments.

Note 9 – Contingencies

Federal Grants - The OSA has received federal grants for specific purposes that are subject to audit by the grantor agencies. Entitlements to these resources are generally conditional upon compliance with the terms and conditions of grant agreements and applicable federal regulations, including the expenditure of resources for allowable purposes. Any disallowance resulting from a grantor audit may become a liability of the OSA. The OSA estimates that the ultimate disallowance pertaining to these grants, if any, will be immaterial to its overall financial condition.

STATE OF MISSISSIPPI
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Year Ended June 30, 2006

Litigation - The OSA is party to legal proceedings, many of which occur in the normal course of governmental operations. The OSA's legal counsel believes that ultimate liability resulting from these lawsuits will not have a material adverse effect on the financial condition of the OSA.

STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
Required Supplementary Information
Budgetary Comparison Schedule – Budget and Actual (Non-GAAP Basis)
General Fund
Year Ended June 30, 2006

	Original Budget	Final Budget	Actual (Budgetary Basis)	Variance with Final Budget Over (Under)
Revenues				
OSA special funds	\$ 4,242,828	\$ 4,627,931	\$ 3,100,447	\$ (1,527,484)
State general fund appropriations	5,277,475	5,277,475	5,277,475	-
State budget contingency fund	190,173	190,173	190,173	-
Federal sub-grant		731,170	383,821	(347,349)
Total revenues	<u>9,710,476</u>	<u>10,826,749</u>	<u>8,951,916</u>	<u>(1,874,833)</u>
Expenditures				
Salaries and benefits	8,069,542	8,472,291	7,143,683	(1,328,608)
Travel and subsistence	722,591	762,232	667,268	(94,964)
Contractual services	811,375	1,311,545	1,000,191	(311,354)
Commodities	78,599	126,458	112,140	(14,318)
Capital outlay	26,615	152,469	81,104	(71,365)
Subsidies, loans and grants	1,754	1,754	1,634	(120)
Total expenditures	<u>9,710,476</u>	<u>10,826,749</u>	<u>9,006,020</u>	<u>(1,820,729)</u>
Excess of revenues over(under) expenditures	-	-	(54,104)	(54,104)
Budgetary Fund Balance - Beginning	<u>-</u>	<u>-</u>	<u>1,496,661</u>	<u>1,496,661</u>
Budgetary Fund Balance - Ending	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,442,557</u>	<u>\$ 1,442,557</u>

The accompanying notes to the required supplementary information are an integral part of this statement.

STATE OF MISSISSIPPI
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Required Supplementary Information
Notes to Required Supplementary Information
Year Ended June 30, 2006

The Budgetary Comparison Schedule - Budget and Actual (Non-GAAP Basis) – General Fund presents the original budget, as well as comparisons of the final budget with actual data on a budgetary basis. The OSA’s basis of budgeting is the accrual basis.

Since accounting principles applied for purposes of developing data on a budgetary basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of differences between budgetary and GAAP presentations for the year ended June 30, 2006 is presented below:

Net change in budgetary fund balance	\$	(54,104)
Adjustments:		
Lapse period revenues are not treated as assets and in the financial reporting period		<u>(50,545)</u>
Net change in GAAP fund balance	\$	<u>(104,649)</u>



INDEPENDENT AUDITORS' REPORT
ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF
FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS

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State of Mississippi Office of the State Auditor
Jackson, Mississippi

We have audited the accompanying financial statements of the governmental activities and the agency fund information of the State of Mississippi Office of the State Auditor, as of and for the year ended June 30, 2006, which collectively comprise the State of Mississippi Office of the State Auditor's basic financial statements and have issued our report thereon dated October 20, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the State of Mississippi Office of the State Auditor's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the State of Mississippi Office of the State Auditor's financial statements are free of

material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Governmental Auditing Standards*.

This report is intended solely for the information and use of management, federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Grantham, Poole, Russell, Reitano, Arrington & Cunningham, PLLC

Jackson, Mississippi
October 20, 2006